

Press Release

The Jammu And Kashmir Bank Limited

December 18, 2020

Rating Reaffirmed



Total facilities	Rs. 1600.00 Cr.
Total BASEL III Compliant Tier-2 Bonds	Rs. 1050.00 Cr.
Long Term Rating	ACUITE AA- /Stable (Reaffirmed)
Total BASEL III Compliant Additional Tier-1 Bonds	Rs.550.00 Cr.
Long Term Rating	ACUITE A+ /Stable (Reaffirmed)

* Refer Annexure for details

Rating Rationale

Acuite has reaffirmed the long-term rating of **'ACUITE AA-' (read as ACUITE double A minus)** on the Rs.1050.00 Crore Non-Convertible Basel III Compliant Tier-2 Bonds of 'The Jammu And Kashmir Bank Limited (J&K Bank)'. The outlook is **'Stable'**.

Further, Acuite has reaffirmed the long-term rating of **'ACUITE A+' (read as ACUITE A plus)** on the Rs.550.00 Crore Basel III Compliant Additional Tier-1 Bonds of The Jammu And Kashmir Bank Limited (J&K Bank). The outlook is **'Stable'**.

The rating takes into account the high strategic importance and pivotal position of the bank in the Jammu & Kashmir (J&K) region, this is reflected in the strong ownership and demonstrated capital support from the Government of J&K. The bank continues to receive support from the Govt. of Jammu & Kashmir, the recent infusion of INR 500 cr tier I capital helps the bank to improve its capitalization. CRAR improved to 11.86% as on Sep 30, 2020 from 11.40% as on Mar 31, 2020. The rating also factors the healthy base of low cost deposits and adequate marked by Current Account and Savings Account (CASA) ratio of 53.3% as on Sep 30, 2020.

The rating is constrained by the bank's moderate asset quality, expected pressure on earning profile amidst the sharp increase in credit cost and relatively small scale of operations with high regional concentration. Acuite has assigned a lower rating on the AT1 bond programme as compared to that of the Tier-2 bonds in line with its criteria of notch down for such instruments. Under Basel III guidelines, AT1 bonds carry higher risk features including the discretion of coupon payments in a weak capital scenario and principal loss absorption in part or full at the 'point of non-viability (PONV)' of a bank.

About the bank:

The Jammu & Kashmir Bank Limited was established in 1938 as a scheduled commercial bank. J&K Bank is a public sector bank with Government of Jammu & Kashmir as a promoter holding 68.18% stake in the bank as on September 30, 2020. JKB has a branch network of 955 branches (792 in region of Jammu and Kashmir and Ladakh and remaining spread across rest of India (ROI)). The bank has been listed on BSE and NSE since 1998.

Analytical Approach

Acuite has adopted the consolidated approach while assessing the business and financial risk profiles of JKB along with its subsidiary JKB Financial Services Limited. Additionally, the majority Government ownership and the ongoing support from the Government of Jammu & Kashmir has been factored in the rating. Acuite has maintained a differential rating of one notch between the Proposed Non-Convertible Basel III Compliant Tier 2 Bond and Proposed Non-Convertible Basel III Compliant Tier 1 bonds. The differential in rating is due to the higher loss absorption characteristics associated with the Tier-1 bond.

Key Rating Drivers

Strengths

- **Pivotal position in the Jammu & Kashmir region**

The Jammu & Kashmir Bank was established in 1938. With a track record of over eight decades, it holds a key position in the UT of Jammu & Kashmir. J&K Bank's deposit base as on Sep 30, 2020 was Rs. 1.00 lakh Crore indicating a 88% share in the overall deposits from the region. Similarly, J&K Bank accounted for 67% of the overall credit in the region. J&K Bank is also the preferred banker for all the J&K State Government enterprises and employees.

Being the largest bank in the UT it forms an integral part of the UT's economic nervous system. J&K Bank has a branch network of 792 branches (in UT of J&K and Ladakh) being the largest spread branch network within the region. RBI has appointed JKB as the lead convenor bank for the UT of Jammu & Kashmir.

J&K Bank is a scheduled commercial bank, with increase in government of J&K and Ladakh's stake to 68.18% as on Mar 31, 2020 from 59.23% Mar 31, 2019 with the equity infusion of Rs.500.00 Crore. The bank continues to receive support from the Govt. of Jammu & Kashmir, whether in the form of growth or distress funding on an ongoing basis. Given its status as a dominant commercial bank in J&K, J&K Bank is expected to play a key role in the economic development of the region and also act as an implementation vehicle for the various government schemes. Considering the socio-political sensitivity of the region and the pivotal position of the bank in that region, Acuite believes that JKB will be strategically important for the Government and it will continue to support the bank through regular financial and managerial support.

- **Healthy base of low cost deposits**

Based on its extensive branch network in the J&K region, the bank has been able to mobilise deposits from a large retail base which forms ~79% of its funding profile. The bank maintained a healthy current accounts savings accounts ratio of 53.3% as on Sep 30, 2020 and 53.6% as on Mar 31, 2020 which compares favorably with the CASA ratios of some other leading banks like SBI (@ 45.2%), HDFC Bank (@40.1%), BOB (@45.2%) as on June 30, 2020. Besides deposits from general public, the bank is also the preferred banker for J&K State run enterprises and employees. ~21% of JKB's deposits come from J&K Government run enterprises and employees.

The continued access to low cost deposits has resulted in robust Net Interest Margins (NIM) for J&K Bank ranging between 3.9% – 4.3% over the past three years. J&K bank reported profit of Rs.40.00 crore in H1FY2021 against the loss of H1FY2020.

Acuite believes that the steady flow of retail deposits and the established retail franchise augurs well for the future profitability of the bank.

Weaknesses

- **Susceptibility to socio-political climate in the Jammu & Kashmir region**

The state of Jammu & Kashmir was formed in 1948, and was accorded special status under Article 370 in 1954. The region Jammu & Kashmir since then has been subject to two major wars and various socio-political hindrances, which has frequently hampered the livelihood and thus economy of the region. Recently, Union of India revoked the special status of Article 370 accorded to the then state of Jammu and Kashmir and reorganized it into UT of Jammu & Kashmir and Ladakh. The bank still relies on the J&K region for major part of its business (88% of deposits, 66% of advances and 83% of branches).

The region has always been a subject of dispute with other countries and hence has always exhibited high degree of social and political volatility. Any continuation of high social instability is likely to result in lower levels of activity in respect of sectors like tourism which are the major thrust areas for the government.

Acuite believes that the banks growth trajectory and future operating performance will depend upon the continued government focus on providing a healthy operating environment in the J&K region, thereby paving the way for attracting fresh investment and sustainability of existing business.

- **Moderate asset quality**

The asset profile of the bank can be classified into two distinct segments, the retail loan book is mainly located within the UT of Jammu & Kashmir and Ladakh while the corporate loan book mainly lies in the Rest of India (ROI). Agriculture and tourism being the major economic drivers of the UT, is impacted by Covid-19 and unrest due to socio-political developments. This would result in delinquencies and restructuring of loans in the near term. The disruption in activities in the Kashmir Valley post changes in political dispensation, resulted in unrest and consequently increase in delinquencies in J&K Bank's retail portfolio. As on Sep 30, 2020 the gross non-performing assets (GNPA) from the retail portfolio stood at 2.9% of overall retail portfolio from 1.2% as on March 31, 2019.

32% of J&K Bank's book is from corporate advances, this portfolio has witnessed major increase in delinquencies over the past few fiscals. Corporate book GNPA rose from 16.6% of the corporate book as on

Mar 31, 2019 to 18.4% as on Mar 31, 2020. Overall GNPA stood at 10.97% as on Mar 31, 2020 as against 8.97% as on March 31, 2019. Further, GNPA improved to 8.87% as on Sep 30, 2020. The upgradations and recoveries improved in FY2020. The bank, however, maintained a provisioning coverage of 79% as on Mar 31, 2020. The bank has now increased its lending in Agriculture and SME segments.

Off the overall GNPA's 68% were from the Top 15 NPA accounts, major portion of the NPA accounts were from single borrower group. As per Acuite discussions with the bank, the bank plans to decrease its large ticket exposure (i.e. exposures above Rs. 200-300 Cr. in order to avoid impact of delinquency in such wholesale exposures).

The increase in delinquencies has also resulted in higher credit costs, moderation in profitability and increase in losses. Loss for FY2020 stood at Rs.1183.39 Cr. CRAR has declined significantly from 12.46% as on March 31, 2019 to 11.40% as on March 31, 2020. On account of capital infusion, it has improved and stood at 11.85% as on Sep 30, 2020

Acuite believes that lowering of credit costs (due to lower slippages) and consequent improvement in profitability will be key monitorables.

Rating Sensitivity

- Increase in asset quality pressures and continued losses;
- Significant improvement in asset quality;
- Definite documented confirmation from the Government regarding willingness to support the bank for its growth/distress capital needs.

Liquidity Position: Strong

JKB's asset-liability tenure is well matched with no cumulative negative mismatches up to the three-year bucket as on Sep 30, 2020. The bank had high current account savings account ratio of 53.3% for 6MFY2021 (FY20: 53.6%). The bank's liquidity coverage ratio was about 361% at 6MFY2021 against the regulatory requirement of 100%. The excess SLR stood at Rs.9795 Crore as on Sep 30, 2020 as against Rs.4230 crore as on Mar 31, 2020. The increase in excess SLR ensures the liquidity buffer available with the bank.

Outlook: Stable

Acuite believes that JKB will maintain a 'Stable' outlook on the back of continuing support from Government of Jammu & Kashmir and its pivotal position in the region of Jammu and Kashmir. The outlook may be revised to 'Positive' in case JKB is able to demonstrate a significant and sustainable improvement in asset quality, profitability and capital adequacy parameters coupled with stated intent of the Government to support the bank. The outlook may be revised to 'Negative' in case the bank faces challenges in attaining a significant improvement in asset quality, profitability and capital adequacy parameters.

About the Rated Entity - Key Financials

Parameters	Unit	FY20 (Actual)	FY19 (Actual)
Interest Income	Rs. Cr.	8446.29	7675.56
Interest Expense	Rs. Cr.	4739.24	4291.13
Profit After Tax (PAT)	Rs. Cr.	-1183.39	463.85
Deposits	Rs. Cr.	97785.83	89636.83
Net Advances	Rs. Cr.	64399.07	66271.51
Investments	Rs. Cr.	22990.47	23140.50
Capital Adequacy	(%)	11.40	12.46
Return on Average Assets (RoAA)	(%)	-1.13	0.49
Gross NPA	(%)	10.97	8.97
Net NPA	(%)	3.48	4.89

Status of non-cooperation with previous CRA (if applicable)

None

Any other information

None

Material Covenants

None

Applicable Criteria

- Banks and Financial Institutions: <https://www.acuite.in/view-rating-criteria-45.htm>
- Financial ratios and Adjustments: <https://www.acuite.in/view-rating-criteria-53.htm>
- Default Recognition: <https://www.acuite.in/view-rating-criteria-52.htm>

Note on complexity levels of the rated instrument

<https://www.acuite.in/view-rating-criteria-55.htm>

Rating History (Upto last three years)

Date	Name of the Facilities	Term	Size of the Issue (Rs. Cr.)	Ratings/Outlook
12 Jun, 2020 (Erratum)	Proposed Bond	Long Term	1050.00	ACUITE AA-/Stable (Assigned)
	Proposed Bond	Long Term	550.00	ACUITE A+/Stable (Assigned)
03 Mar, 2020	Proposed Bond	Long Term	1050.00	ACUITE AA-/Stable (Assigned)
	Proposed Bond	Long Term	550.00	ACUITE A+/Stable (Assigned)

*Annexure – Details of instruments rated

ISIN	Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Cr.)	Ratings/Outlook
-	Proposed Basel III Compliant Tier-2 Bonds	-	-	-	1050.00	ACUITE AA-/Stable (Reaffirmed)
-	Proposed Basel III Compliant Additional Tier-1 Bonds	-	-	-	550.00	ACUITE A+/Stable (Reaffirmed)

Contacts

Analytical	Rating Desk
Mohit Jain Vice President – Rating Operations Tel: 022- 4929 4071 mohit.jain@acuite.in Simranjeet Kaur Analyst - Rating Operations Tel: 022- 4929 4072 simranjeet.kaur@acuite.in	Varsha Bist Senior Manager - Rating Desk Tel: 022-4929 4021 rating.desk@acuite.in

About Acuité Ratings & Research:

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